5 Things to Know About China’s Currency Devaluation

China on Tuesday devalued its currency in a way that left it 1.9% weaker versus the U.S. dollar. The move will likely have a ripple effect through financial markets as well as in politics, as China is the world’s largest trader and the yuan is increasingly used overseas. Here are five things you need to know about Beijing’s latest move.

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By
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1 What did China do?

China tightly controls the value of its currency by setting a daily rate for the yuan versus the dollar. In China’s domestic market, traders are allowed to push the yuan 2% stronger or weaker for the day. But the People’s Bank of China often ignores those market signals when it sets the next day’s rate, sometimes setting the yuan stronger versus the dollar when the market is signaling it sees the yuan as weaker. The central bank said it will now take the previous day’s trading into account and it attributes that move to Tuesday’s sharp drop.

2 Why did China do it?

In its statement, the PBOC said it wants to bring the yuan more in line with the market. But the move also comes as China’s important export sector has weakened and overall economic growth looks sluggish. Over the weekend, Chinese customs officials said July exports fell 8.3% compared with a year ago. A weaker currency helps China’s exporters sell their goods abroad.

3 What does this mean for markets?

The most immediate effect is that it signals to the world that Beijing thinks the Chinese economy is sputtering. The move suggests China is looking for ways to get it going again. But it also has major implications for the U.S. and other countries that trade with China because it puts their companies at a disadvantage. In the U.S., it will likely reignite criticism that Beijing keeps the currency artificially low to help its own manufacturers a charge that could get added impetus during the presidential election campaign.

4. What does this mean for markets?
The move puts pressure on other central banks around the world to push down their own currencies to help their own exporters and to prevent destabilizing capital flows. The move could hurt commodities markets because it signals potential weak demand from China. It could also accelerate capital outflows out of China, especially if investors expect further devaluations.

- 5 What’s next?

The move could add to tensions ahead of Chinese President Xi Jinping’s visit to the U.S. and his meetings with President Barack Obama, which is set for late September. It could also complicate China’s efforts to get the yuan added to a basket of currencies tracked by the International Monetary Fund’s efforts aimed at giving the yuan greater acceptance abroad. Longer-term, the move raises questions about Beijing’s pledge to liberalize its economy. On one hand, making the yuan more market-driven is a step in that direction. But the move also appears to be designed to help exporters, at a time when China has been looking for other, more dependable sources of growth.

**China’s devaluation of its currency**

What’s happening to China’s yuan?

The yuan usually changes in value a fraction of a percentage point in a day. But on Tuesday, China’s central bank abruptly devalued the yuan by nearly 2 percent—the largest single-day drop since 1994. On Wednesday, China’s central bank devalued it by another 1.6 percent and on Thursday, 1.1 percent. Since Friday, when the yuan took a turn and appreciated .1 percent, the yuan has stabilized.

Global stock markets have been on a roller coaster ride since Tuesday, as the world tries to understand what the currency move means.

Why would China weaken its currency?

First, a bit of background.

China’s economy, the world’s second largest after the U.S., has been slowing down. For decades, the country had what many said was an uns sustainable growth rate. In 2014, investments made up 48 percent of economic activity; in most countries that number is between 15 and 30 percent. Recently, there has been a slowdown in property investment, construction has lagged, and consumer spending is down. Then in June, China’s stock market crashed, and the government stepped in to reign in selling. In less than a month, shares fell by nearly a third.

China’s growth rate has dropped to 7 percent, a high number almost anywhere in the world, but low in a country that averaged 10.6 percent growth in 2010 and some economists wonder if the real number is actually lower.

Unlike most countries that allow the value of their currency to be determined in world markets, China’s government uses the U.S. dollar as a benchmark against which they manage their currency’s value—a policy dating back to the mid 90s. However, in the past two years, as the U.S. dollar
appreciated in value, China’s economy slowed, making it increasingly difficult for the government to justify pegging the yuan to the dollar.

The move to depreciate the yuan was twofold. First, with exports slumping, officials were under pressure to try to boost them. Chinese products are cheaper as a result of the depreciation, making it more appealing for other countries to import Chinese products.

Second, China has been under a lot of pressure by the United States and the International Monetary Fund to allow their currency to be valued by the market. It’s part of broader financial market reforms by China to rebalance its growth and generate more consumption-driven growth. Having China grow in a balanced and sustained manner is good for China and the world, said Eswar Prasad, professor of trade policy at Cornell University and a former IMF official. And that’s in America’s interest: if China increases domestic consumption, they will import more from the U.S.

**Hold on, I don’t understand. Is China manipulating its currency, or is it allowing it to fall according to the market?**

The 2 percent move was something that was orchestrated by the Chinese central bank, said Prasad, referring to the Tuesday’s devaluation. Then they allowed the market to decide from there. The depreciation was something that the market wanted.

A slowing economy would normally depreciate a country’s currency. The nearly 2 percent drop orchestrated by the People’s Bank of China jumpstarted a move in the direction the market had been trying to pull it. The central bank might allow the currency to depreciate further, but they have also said that they won’t allow it to go too much further. On Thursday, in an attempt to quell growing concerns, Chinese officials said that their currency is not in free fall and that the bank maintains the power and authority to intervene and stabilize the yuan if need be. On Friday, the People’s Bank of China appeared to do just that, stabilizing the yuan in order to quell concerns from global markets as well as to smooth things out in their own financial markets, said Prasad.

In other words, the People’s Bank of China has adopted a managed float regime.

**OK, so how is this affecting the global economy?**

Well, China’s timing doesn’t exactly suit the rest of the world. Stock markets fell globally initially, rebounding a bit on Thursday and again on Friday following China’s assurance that the yuan isn’t in a free fall. Businesses that compete with China for exports or that have significant sales in China saw their share prices take a hit. Last week European stocks had their worst week in six but bounced back on Monday.

[China is] doing exactly what the U.S. wanted at a time that is convenient for them and not for the global economy, Prasad said. And when you have an economy as big as China’s, it affects the rest of the world.

So you have the world’s second largest economy, which has been this big tailwind for global growth—suddenly sputtering, Mike McDonough, chief global economist at Bloomberg Intelligence, told Judy Woodruff on the PBS NewsHour Wednesday. So this tailwind is becoming a headwind. That’s the real concern. It’s not the devaluation.
The devaluation signals that something is wrong, and that’s what sent stock markets on their roller coaster ride, Prasad said.

First, by devaluing their currency, people thought “China was throwing in the towel.” That is, the Chinese central bank must know something that rest of the world does not, that the Chinese economy must be worse than we think.

Second, countries fear a currency war. “There’s a lot of volatility in stock markets around the world, because they fear that other countries will deprecate their currency,” says Prasad. The cheaper a country’s currency, the more competitive its exports. With such a weakened yuan, China is a “fierce competitor” more so than ever.

It’s possible that countries will deprecate their own currencies in order to compete with China, but the likelihood of a currency war depends on whether or not the yuan continues to deprecate.

Who’s taking the biggest hit?

Canada, New Zealand, Australia, Korea, Thailand, and Malaysia are likely to be hardest hit. They export a lot to China, but with a weakened Chinese economy, there is less demand for their goods. Korea, Thailand and Malaysia are facing a double whammy in that they often compete with China to export cheap goods to the rest of the world.

What does this all mean for U.S. markets?

Caught off guard, stock markets opened lower on Tuesday and dropped even more Wednesday, with the Dow Jones Industrial Average dropping 277 points before heading back to its original standing. On Thursday, likely in response to China’s government saying they will not allow a free fall of the yuan, the market steadied. And since Friday, with the stabilization of the yuan, it appears that markets have gotten off the roller coaster ride for now at least and are returning their attention to other matters.

Still, there are lingering concerns that the devaluation of the yuan could hurt the recovery for U.S. companies that export to China, because their products will be more expensive for Chinese consumers to buy. Additionally, exports from China are going to be cheaper for U.S. consumers, which is going to hurt U.S. manufacturers.

Not only that, China has been the biggest driver of global growth since the Great Recession, so if China is slowing down, the world may be as well.

That sounds scary! What does this mean for me?

“At this stage it’s way too early to tell,” Prasad said, “short term is a little dicey, long term looks a little better.”

If a currency war does begin, it might not necessarily hurt U.S. consumers. If everyone deprecates the value of their currencies, the U.S. dollar will grow stronger. A stronger dollar means cheap imports, less expensive vacations abroad and lower interest rates. So even if the Fed raises interest rates in the fall, Prasad predicts that they will stay low in the long term, which would be good for mortgages and auto loans.
Cheap imports and low interest rates are going to be a big benefit to the average American household, Prasad explained. So the benefits are going to be widespread, but the pain is going to be very concentrated in some sectors that could face very significant job losses and loss of economic momentum.

Is China manipulating its currency? The Big Mac Index says yes

BY Kristen Doerr  July 18, 2015 at 11:53 AM EDT

What can the Big Mac Index tell you about your nation’s currency? Photo by Jason Alden/Bloomberg via Getty Images

On Thursday, the Economist came out with 2015’s Big Mac Index.

What, you ask, is the Big Mac Index? It’s just what it says—an annual index of McDonald’s Big Mac, priced in different currencies.

The Economist began the Big Mac Index back in 1986 as a light-hearted measurement of “whether currencies are at their correct level.” It stuck.

The Big Mac Index is based on the economic concept of purchasing power parity, which tries to adjust prices in different countries to account for differences in exchange rates. To oversimplify, if the dollar is worth about 6 Chinese yuan, which it is at the moment, an identical item in China should cost roughly six times as many yuan as dollars in America. And since a Big Mac is sort of identical anywhere in the world, argues The Economist, its price ought to reflect the exchange rate of the currency in which it’s being sold and little else.

Back in 2004, NewsHour economics correspondent Paul Solman did a story on the falling dollar and sat down with The Economist’s Tom Easton to understand why the Big Mac was a reliable metric.

Now look at the chart and notice this year’s results. A Big Mac in China in July of 2015, priced in dollars at the current dollar-yuan exchange rate: $2.74. The average price in America this month? $4.79. They ought to be nearly the same. In fact, the Chinese Big Mac is selling at 43 percent less than its American progenitor. To The Economist, this is compelling evidence for what critics of Chinese economic policy have long argued: that the Chinese have manipulated the yuan, keeping it artificially low in order to increase their exporting capabilities. Or, as the magazine puts it: “the raw Big Mac index says that the yuan [is] undervalued by 43%.”

And what about the euro, which has been falling fast since the Greek crisis re-erupted a few months ago? According to the Index, because Big Macs are also now less expensive in Europe than America, exchange-rate adjusted, the U.S. dollar is overvalued by almost 20 percent against Europe’s common currency. And what country boasted the cheapest Big Mac in the world? Venezuela, at a mere 67 cents. That suggests that although Hugo Chavez’s former fiefdom has been plagued by volatile politics and plummeting oil prices, its currency may be something of a bargain these days. Switzerland, on the other hand, continues to have the world’s most expensive Big Mac. Visit a McDonald’s there, and you’re ponying up $6.82 for your 495 calories.
Now Burgernomics (and yes, that’s the term) has its limitations. For one thing, Big Macs are not identical everywhere. For example, the American Big Mac must be fatter than the Swiss, weighing in at an unhealthy 515 calories, according to MyFitnessPal, the diet app. And purchasing power parity rates are difficult to determine for a number of reasons besides portion size, well summarized here. Still, the Big Mac Index has been a somewhat reliable indicator of currency over- and undervaluation in the past. And it’s fun to look at, regardless.


Eight reasons why China’s currency crisis matters to us all

The Chinese leadership’s devaluation of the yuan delivered a temporary shock to financial markets, but its longer-term effects may be felt around the globe.

After China unexpectedly devalued its currency last week, one City economist shrugged despairingly and said: “It’s August.” While it meant to be a time for heading for the beach or kicking back in the sunshine with the kids, August has often witnessed the first cracks that presaged what later became profound shifts in the tectonic plates of the global economy from the Russian debt default in 1998, to what Northern Rock boss Adam Applegarth called “the day the world changed,” when the first ripples of the credit crunch were felt in 2007; to August 2011, when ratings agency Standard and Poor’s sent shockwaves through financial markets by stripping America of its triple-AAA credit rating.

Taking the long view, last week’s devaluation by China, which left the yuan about 3% weaker against the dollar, was relatively modest—sterling had lost 16% of its value in 1967 when Harold Wilson sought to reassure the British public about “the pound in your pocket.”

But China’s decision represented the largest yuan depreciation for 20 years; and the ripples may yet be felt thousands of miles away. So what difference will it make to the rest of the world?

1. It could be serious

China’s devaluation may be best seen as a distress signal from Beijing policymakers — in which case the world’s second-largest economy may be far weaker than the 7% a year growth that official figures suggests. China has been trying to engineer a shift from export-led growth to an expansion based on consumer spending — which suggests some policymakers may be losing patience with that strategy, and reaching for the familiar prop of a cheap currency. Nobel prize-winning economist Paul Krugman described the decision as “the first bite of the cherry,” suggesting more could follow, and in a reference to Chinese president Xi Jinping, warned that such a modest move gave the impression that, when it comes to economic policy Xi-who-must-be-obeyed has no idea what he is doing.
If its economy really is much weaker than Beijing has let on, it would be alarming for any company hoping to export to China — something firms in Britain have been encouraged to do in recent years, to lessen reliance on the stodgy European economies. China was the sixth-largest destination for British exports last year. China will remain a vast market; but it may not be quite such a one-way bet as some analysts have suggested. And when it comes to the challenges facing Chinese policymakers, Russell Jones, of consultancy Llewellyn Consulting says: “The potential for getting this wrong is quite high.”

2. A less costly Christmas

China has been trying to shift from being a vast factory producing cut-price consumer goods for the rest of the world. Yet glance at the label on almost any T-shirt or toy and it’s still likely to read “Made in China.” A country’s currency is not the only determinant of how much its goods will cost when they reach the high street: Chinese wages have been rising, making its products less competitive, and the price of raw materials and shipping is also important. However, the devalued yuan will force China’s Asian rivals, such as Indonesia and South Korea, to compete even harder in response; and the result may be a few pence off the price of Chinese-made Christmas presents. Martin Beck, of consultancy Oxford Economics, says, “Almost 9% of the UK’s goods imports come from China, a share that has doubled over the last decade.” So there will be a direct disinflationary effect from cheaper imports.

3. Cheaper petrol at the pump

China’s apparently insatiable demand for natural resources has been a key factor supporting the price of oil in recent years. So fears that China’s economy is in trouble tend to undermine oil prices and that probably means cheaper petrol in Britain. Of course, there are other factors, including strong oil production in the US; but global oil prices resumed their decline last week following China’s move, dipping back below $50 a barrel. In coming months, weak Chinese demand could force down the cost of many commodities, from oil to iron ore.

4. Delayed rate rises

Central bankers in the US and the UK have been issuing warnings for months that, with growth strengthening, they are preparing to start pushing up interest rates reversing the emergency cuts made in the global credit crunch. Mark Carney, the Bank of England governor, has suggested “the turn of the year might be the moment to consider tightening monetary policy (ie raising rates); Janet Yellen at the US Federal Reserve has signalled that an increase could come as early as September.” However, if the cheaper yuan cuts the price of imports, this will undermine inflation, which is already at zero in the UK; and could delay a rate rise. A renewed bout of market turbulence as global investors assess the implications of China’s decision could have the same effect.

5. Deflation, deflation, deflation

In the short term, lower-than-expected borrowing costs will benefit indebted consumers in the west including Britain’s mortgage-holders. But some analysts believe China’s decision is the latest evidence of a deep-seated lack of demand in the global economy, which will unleash deflation. Brief periods of falling prices particularly if concentrated among one or two commodities can be good news; but economists fret about periods of persistently falling prices, which can undermine spending
and investment and feed through to wages, as consumers and businesses delay spending, expecting goods to be even cheaper in future. And if a fresh downturn does come, central bankers have little ammunition left to tackle it, since interest rates in the US, the UK and Europe are already on the floor. Economist Ann Pettifor, of thinktank Prime, who foreshadowed the credit crunch in her 2006 book, The Coming First World Debt Crisis, believes the developed economies face some of the challenges felt by Japan during its “lost decade” when it suffered both deflation and weak demand. But unlike Japan, many developed economies, not least the UK, would enter any new crisis under a heavy burden of borrowing, Pettifor says, raising the spectre of the kind of debt trap identified by the US economist Irving Fisher in the wake of the Great Depression. Not everyone is so pessimistic, and Carney has shrugged off the idea that deflation is a threat in the UK; but as Neil Mellor, of BNY Mellon, put it in a research note on Friday, “as we watch and wait, the market will be anxiously aware that a sustained depreciation could have ramifications across the globe by shifting the inflation dynamic at a most inopportune time.”

6. Tough times for Oz

Australia has experienced an impressive economic boom in recent years on the back of selling natural resources, including coal and iron ore, to its Asian neighbours, and China accounts for more than a quarter of its exports. So weakness in the Chinese economy is bad news for Australia. Research by consultancy Oxford Economics last week, which modelled the impact of a 10% Chinese devaluation, accompanied by a sharp slowdown, suggested other hard-hit countries could include Brazil, Russia, Chile and Korea.

7. Even more pain for Greece

If the Chinese devaluation does bring what one City analyst, Albert Edwards, last week called a “tidal wave of deflation” to the global economy, the most vulnerable countries will be those that are heavily in debt because while wages and profits fall in a deflationary period, the value of debts remains fixed, making them harder to service (to pay interest on). And economies where consumer demand and confidence is already weak tend to be hit harder by the reduced spending that deflation can bring. As economists at consultancy Fathom said last week, “peripheral European economies,” not least crisis-hit Greece, fit that definition. Greece is already suffering deflation after repeated cuts in wages and benefits as the government tries to balance the books, and if it worsens, that will only make its gargantuan debts—worth more than 170% of the size of the economy—harder to service.

8. Currency wars

Beijing’s move was ostensibly offered as part of measures to open up its financial system, and allow foreign exchange markets more say over the value of the yuan because something America has long demanded as evidence that China is genuinely open to financial reform. The International Monetary Fund described the move as welcome. But the devaluation was nevertheless greeted angrily in Washington. New York senator Chuck Schumer said: “For years, China has rigged the rules and played games with its currency, leaving American workers out to dry. Rather than changing their ways, the Chinese government seems to be doubling down.” Republican senator and former US trade representative Rob Portman accused China of trying to gain an unfair trade advantage over America through “currency manipulation” just as the US is negotiating an important trade agreement, the Trans-Pacific Partnership, with a number of China’s rivals, including Japan.
If Beijing allows the yuan to decline further in coming months, it could increase trade tensions, or even a “currency war,” in which the world’s big trading blocs face off in a beggar-thy-neighbour battle to seize the largest possible share of global consumer demand. For now, a 4% devaluation in the yuan is more of a hairline crack in the world economic order than a seismic shift; but policymakers will be weighing up its consequences long after they return from their summer break.

• This article was amended on 20 August 2015. Xi Jinping is president (not prime minister) of the People’s Republic of China.

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How China's Currency Policies Will Change the World

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There were several reasons behind China's decision, but it nevertheless came as a surprise to many. In search of stability, China has tied its currency to the U.S. dollar since 1994, usually at a low value relative to the dollar. During the 2000s, the connection helped China keep its exports competitive, with the developed world consuming its output. The West's economic collapse in 2008 meant that this model could no longer function, and China began trying to grow consumption levels so that the domestic consumer might come to fill the hole left by the faded international market.

Changing China

Transforming from an export-led economic model to a consumption-led one could be described as changing from being like Germany to being like the United States, and China has tried to reproduce some of the advantages that the United States has created for itself in the same role. One of those advantages is the dominant position of the U.S. dollar in world trade, which means U.S. consumers can go deeply into debt and global demand for dollars will delay the moment at which this comes to a head by those debts being catastrophically called in. Thus China sought to grow international usage of the yuan, making strides in its attempts to do so. The next step would be for the yuan to be accepted into the International Monetary Fund's "currency," the Special Drawing Right. However, the IMF has said that China would need to liberalize its currency before such a step could take place. The IMF makes the decision every five years, with one originally set for November this year, though the institution recently announced that any changes will not be implemented until October 2016.

Meanwhile, the peg to the dollar aided China's strategy as the strengthening dollar over the past two years enabled the yuan to rise alongside it relative to the world's other floating currencies, empowering Chinese consumers and helping the changeover from an export- to consumption-based economy. But low global demand has not created a good climate for such change, and growth has been unsteady during this period, slipping to 7 percent this year. The baton pass from an export-driven to consumption-driven economy is risky, and exports need to hold up long enough for the Chinese consumer ðœ and building blocks such as the reserve currency ðœ to develop. When export numbers for July showed an 8.3 percent fall year-on-year, all signs seemed to point toward a loosening of controls, which would both please the IMF and, if the Chinese currency continued to weaken as many in the market expected it to, help boost exports.
The Repercussions

In the globalized world, where every economy is interconnected with every other economy, the effects of a shift like China's can be felt everywhere. The world's largest economies have tended to move in concert throughout modern financial history, with central banks choosing to tighten or loosen interest rates, often in quick succession. But actions over the past two years have diverged from the rule. While one group is now considering raising interest rates for the first time since 2008, another group is still pursuing quantitative easing programs, which are partly designed to devalue currencies and stimulate growth. China's dislocation from the dollar, particularly if the yuan devalues further against the dollar, moves the country from the first group toward the second, with clear consequences:

and capital has flowed from emerging markets to the United States in anticipation.

Only sporadic growth and low productivity levels, along with stubbornly low inflation figures in the U.S. and U.K., have caused their central banks to delay the rate rise, but recent strong job creation figures led many in the market to expect the United States to make the change in September 2015 (and the United Kingdom in early-to-mid 2016). The U.S. economy does not particularly rely on exports, insulating it from some of the drawbacks of currency strength, which usually hurts exports. But China's latest move creates another currency against which the dollar can appreciate. Now, a rate hike would likely strengthen the dollar even more, to the extent that it might become an issue for the U.S. economy. China's reshuffle, then, may have changed the answer to the biggest financial question of the year; market expectations for the rate rise have slipped back to December and may even move to 2016.

Emerging Markets

Emerging markets have suffered a torrid few years. Commodity exporters in Asia, Africa and Latin America enjoyed a boom period between 2000 and 2008, when China was consuming their raw materials as part of its production machine and Chinese investment sustained prices for a few years after. But global commodity prices have fallen since 2011, with the economies of Brazil, Nigeria, Russia and several parts of Asia suffering the most, as evidenced by their steadily falling currencies. The yuan's depreciation reduces China's spending power, and unsurprisingly emerging market currencies have continued to decline. Every time the yuan weakens, it creates more problems for these countries, as many welcomed Western capital during the good times and now have sizable dollar-denominated loans on private balance sheets that are becoming harder to pay back.
**With no international (or domestic) agreements on what constitutes currency manipulation, it’s time world leaders take action.**

With the sudden depreciation of China’s renminbi, it’s worth looking at the link between currency values and trade agreements. China’s currency last week dropped by a cumulative 4.4% against the U.S. dollar, making Chinese exports cheaper and imports into China more expensive by that amount.

The effect on trade can be substantial. With the U.S. average tariff on industrial goods well under 2%, this change in China’s currency value easily swamps most U.S. tariffs. And given the fact that the U.S. dollar was already strong, this move is an added disadvantage to U.S. exports headed for China compared to exports from other countries.

As world leaders continue negotiating what’s poised to be a landmark trade deal across the Pacific Rim, some U.S. lawmakers have responded with criticism:

“Today’s provocative act by the Chinese government to lower the value of the yuan is just the latest in a long history of cheating,” said Republican U.S. Sen. Lindsey Graham, who along with Democratic New York Sen. Chuck Schumer had sought to include a tough provision against currency manipulation in the Trans-Pacific Partnership Agreement (TPP).

China is not a part of the TPP negotiations, but the trade deal has an open architecture—other countries can negotiate accession to the agreement anytime after the current 12 participants conclude the deal. For this reason, and because there was Congressional concern voiced last Spring over currency manipulation during consideration of trade legislation, China’s action has freshened the focus on the linkage of currency values to trade.

The subject is controversial. There is no international (or domestic) agreement on what constitutes currency manipulation. Countries such as Brazil have criticized the U.S. Federal Reserve’s monetary policies (designed to stimulate U.S. economic recovery) for weakening the greenback. U.S. auto companies have complained about Japanese currency manipulation, although the U.S. Treasury has not cited direct intervention in the currency markets (or even indirect intervention—taking the yen’s value down) while Prime Minister Abe has been in office. China’s case is also complicated. The value of the RMB had been rising against the dollar over the last two decades by over 30%. In May, the International Monetary Fund declared that it no longer considered the RMB to be undervalued.

China’s latest currency move has drawn muted responses from the IMF and U.S. Treasury. As quoted in *The New York Times*, the IMF said “China’s new plan for determining the value of the renminbi appears a welcome step as it should allow market forces to have a greater role.” But the IMF also carefully noted that “the exact impact will depend on how the new mechanism is implemented in practice.” The U.S. Treasury’s statement followed a similar line.

Nonetheless, Congress, in the recently passed trade promotion authority, set out as a principal that any trade deal the U.S. negotiates will have zero tolerance for currency manipulation. This negotiating objective, and a companion provision dealing with unfair currency practices, are applicable to TPP.
To be responsive to this Congressional mandate, the U.S. Treasury is working with its TPP country counterparts on a currency understanding. This would provide that finance officials and central bankers meet to promote greater accountability with respect to currency values and to avoid exchange rate manipulation. The proposal is envisaged as a forum for addressing these questions without binding dispute settlement being available to settle differences.

This does not go as far as many in Congress seek, but it is a step in the direction of giving some substance to what in fact has been the international trade rule on exchange rates since 1947: countries are not to undermine their trade commitments by actions they take on exchange rates.

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